



OFFICE OF THE MISSOURI STATE TREASURER

SARAH STEELMAN, Treasurer

I. AUTHORITY

The Constitution and laws of the State of Missouri authorize the Missouri State Treasurer to have custody of all state monies and to invest said monies not needed for the daily operations of the State. The Treasurer has assigned responsibility for the day-to-day administration of this policy to the Director of Investments.

II. INVESTMENT COMMITTEE

The State Treasurer's Office Investment Committee shall be responsible for developing and reviewing the investment process of the State Treasurer's Office within the framework provided by the Constitution and Statutes of the State of Missouri. The State Treasurer's Office Investment Committee shall set and monitor policies, set general strategies and implement necessary monitoring mechanisms.

The Committee will meet regularly to review performance, policy, procedures and legislation.

Members of the Committee shall include:

- State Treasurer
- Director of Investments – Chair
- Assistant State Treasurer
- Director of Banking

III. INVESTMENT ADVISORY COMMITTEE

The State Treasurer will appoint an Investment Advisory Committee made up of investment professionals from around the state. The purpose of the Advisory Committee is to allow investment professionals in the state to lend expertise to this investment process.

IV. PRUDENCE

All participants in the investment process shall act responsibly as custodians of the public trust. The standard of prudence to be applied by the personnel of the Investment Division shall be the “prudent investor” rule, which states, “Investments shall be made with judgement and care, under circumstances then prevailing, which persons of prudence, discretion and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived.”

V. ETHICS AND CONFLICT OF INTEREST

Personnel involved in the investment process shall refrain from personal business activity that could create an appearance of impropriety or could conflict with proper execution of the investment program, or which could impair their ability to make impartial investment decisions. Employees and investment officials shall disclose to the Treasurer any material financial interests in financial institutions that conduct business within Missouri, and they shall further disclose any large personal financial/investment positions that could be related to the performance of the portfolio. Employees and officers shall refrain from undertaking personal investment transactions with the same individual with which business is conducted on behalf of the State of Missouri.

VI. DELEGATION OF AUTHORITY

Authority and responsibility for the management and operation of the investment program is hereby delegated to the Director of Investments, who shall act in accordance with the established written procedures and internal controls for the operation of the investment program consistent with this investment policy. Only the Director of Investments, Investment Analyst, Investment Coordinator and Time Deposit Coordinator positions are authorized to make investments and to order the receipt and delivery of investment securities among custodial security clearance accounts. The Director of Investments shall be responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of subordinate staff.

VII. OBJECTIVES

The primary objective of investment activities shall be legality, safety, liquidity, yield and the provision of a capital base for statewide economic development.

➤ Legality

The State Treasurer’s Office will invest the state’s excess funds only within the legal guidelines set forth by the Constitution and Statutes of the State of Missouri. Any investment alternative outside these guidelines is not permissible. Furthermore, the State Treasurer’s Office seeks to promote and support the objectives of US foreign policy regarding terrorism. Accordingly, investments in companies or their subsidiaries or affiliated entities that are

known to sponsor terrorism or aid the government in countries that are known to sponsor terrorism are prohibited.

➤ Safety

Safety of principal is the foremost objective of the investment program. Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. The objective will be to mitigate credit risk and interest rate risk.

a. **Credit Risk**

The State Treasurer's Office will minimize credit risk, the risk of loss due to the failure of the security issuer or backer, by:

- Establishing a pre-approved list of financial institutions and companies that the State Treasurer's Office will be restricted to when purchasing commercial paper
- Conducting regular credit monitoring and due diligence of these issuers.
- Pre-qualifying the financial institutions and broker/dealers with which the State Treasurer's Office will do business with for broker services and repurchase agreements
- Diversifying the portfolio so that potential losses on individual securities will be minimized.

b. **Interest Rate Risk**

The State Treasurer's Office will minimize the risk that the market value of securities in the portfolio will fall due to changes in general interest rates, by:

- Maintaining an effective duration of less than 1.5
- Holding at least 40% of the portfolio's total market value in securities with a maturity of 12 months or less

➤ Liquidity

The investment portfolio shall remain sufficiently liquid to meet all operating requirements that may be reasonably anticipated. This is accomplished by structuring the portfolio so that securities mature concurrent with cash needs to meet anticipated demand. Furthermore, since all possible cash demands cannot be anticipated, the portfolio should consist largely of securities with active secondary or resale markets.

➤ Yield

The investment portfolio shall be designed with the objective of attaining a market rate of return throughout budgetary and economic cycles, taking into account the investment risk constraints and liquidity needs. Return on investment is of least importance compared to the safety and liquidity objectives described above.

➤ **Provision of a Capital Base for Statewide Economic Development**

The State Treasurer's Office will seek to promote Missouri's economic growth by placing funds on deposit with Missouri financial institutions and in eligible commercial paper and bankers' acceptances issued by Missouri-based companies and/or major employers within the State. As such, the State Treasurer's Office shall consider the overall benefits to the economy and welfare of the State and its citizens through the direct and secondary economic benefits of investments in Missouri. However, such investments shall be subject to the same credit risk guidelines as all other investments, and investment staff shall not be directed to purchase in-state commercial paper or other securities at lower yields than other securities within the same asset class.

The State Treasurer's Office will seek to enhance total portfolio return by means of active portfolio management. The prohibition of speculative investments precludes pursuit of gain or profit through unusual risk. However, trading in response to changes in market value or market direction is warranted under active portfolio management.

VIII. PERFORMANCE

Active management should produce, over a period of time, book yields in excess of a low risk passive benchmark. For management purposes, and for the Investment Committee review, both the book yield and total rate of return will be calculated for the portfolio and compared to the appropriate security market indexes as established by the Committee.

IX. BROKER/DEALER REQUIREMENTS

Investments will be made through banks or securities dealers who have been approved by the Investment Committee. Such securities dealers and banks shall have been subjected to an appropriate investigation by the staff of the State Treasurer's Office, which shall include, among other things, a review of the firm's financial statements and the background of the sales representative. All approved dealers must be fully licensed and registered NASD Broker/Dealers or exempt banks. Criteria used to select securities dealers will include:

- Financial strength and capital adequacy of firm;
- Services provided by firm;
- Research services available;
- Resume, reputation and qualifications of sales representative;
- Due diligence and firm references; and,
- State government expertise.

X. REPORTING

The Investment Division shall report monthly to the Investment Committee on the present status of the investment portfolio. The report will, at a minimum, include the following:

- The market value of the portfolio including realized and unrealized gains or losses resulting from appreciation or depreciation.
- Average weighted yield to maturity and duration of all portfolios as compared to applicable benchmarks.
- Percentage of the total portfolio that each type of investment represents.
- The rating levels for commercial paper and bankers' acceptances. The investment division should also recommend to the committee if the commercial paper or bankers' acceptances should be held or sold in the event of a rating downgrade below the minimum acceptable rating levels.
- Listing of individual securities held at the end of the reporting period.
- At least annually, the realized and unrealized gains or losses resulting from appreciation or depreciation by listing the cost and market value of securities over one-year duration in accordance with Government Accounting Standards Board (GASB) 31 requirements.

XI. PERMISSIBLE INVESTMENTS AND GUIDELINES

A. Investment Types

In accordance with and subject to restrictions imposed by the Constitution and the laws of the State of Missouri, the following list represents the entire range of investments that the Missouri State Treasurer will consider and which shall be authorized for the investments of funds.

1. Time Deposits
 - a. Financial institutions with a physical location in the State of Missouri will be selected as depositories based on but not limited to the following: financial stability, funds availability, loan-to-deposit ratio, community involvement and other relevant economic criteria.
 - b. The maximum maturity of a deposit will be five years as set forth in the statutes.
 - c. The rate of interest to be earned on monies placed in time deposits with Missouri financial institutions will be the same as what is paid on U. S. Treasury securities maturing closest to the time of termination of the deposit as set forth in the statutes.
 - d. A financial institution will be eligible to receive total deposits in an amount not to exceed their equity capital. The State Treasurer's Office may, from time to time, limit the dollar amount of deposits a financial institution may receive due to lack of availability. At no time shall the State Treasurer's Office deposit more than 7.5% of total general time deposits into any single financial institution.

- e. A financial institution's loan to deposit ratio must be in excess of 50% at the time of deposit unless a specific need can be shown by the financial institution for the funds.
 - f. Time deposits (principal and interest) must be collateralized at least 100% with approved securities. The market value of all time deposit collateral will be reviewed on an ongoing, periodic basis to determine collateral adequacy.
2. Linked Deposits
- a. Financial institutions with a physical location in the State of Missouri will be selected based upon financial stability and funds availability.
 - b. Maturity of the deposits will be based upon the statutes' language for maximum maturities of deposit, the borrower's needs, the liquidity requirements and interest rate risk considerations of the State Treasurer's Office and any other relevant economic considerations. This can vary by category of linked deposits.
 - c. The rate of interest to be charged follows the statute language regarding the loan rate to the borrower that is below the normal borrowing rate. However, the minimum rate may not be less than 1%.
 - d. The minimum and maximum amounts of the linked deposit to be placed in each category will be determined by the Investment Committee when these amounts are not specifically stated in the statutes.
 - e. Linked deposits (principal and interest) must be collateralized at least 100% with approved securities. The market value of all linked deposit collateral will be reviewed on an ongoing, periodic basis to determine collateral adequacy.
3. U. S. Treasury and Federal Agency Securities
- a. Treasury and Agency securities with final maturities of five years or less as stated in the statutes may be purchased.
 - b. Treasury and Agency securities must be purchased through approved broker/dealers.
 - c. Agency securities include those specific obligations referenced in (X. B.) that are issued or guaranteed by any agency or instrumentality of the United States Government.
4. Commercial Paper
- a. Commercial paper which has received the highest letter and numeral ranking (A1 / P1) as provided for by Standard & Poor's Corporation (Standard & Poor's) and Moody's Investors Service, Inc. (Moody's).
 - b. Eligible paper is further limited to issuing corporations that have a total commercial paper program size in excess of \$250,000,000 and have long term debt ratings, if any, of "A" or better from Standard & Poor's or Moody's.

- c. Purchases of commercial paper may not exceed 180 days to maturity. The maximum maturity can be further limited by the Investment Committee.
- d. No more than 5% of the total market value of the portfolio may be invested in the commercial paper of any one issuer.

5. Bankers' Acceptances

- a. Bills of exchange or time drafts on and accepted by a commercial bank, otherwise known as bankers' acceptances.
- b. An issuing bank shall have received the highest letter and numeral ranking (A1 / P1) as provided for by Standard & Poor's and Moody's.
- c. Eligible bankers' acceptances are further limited to issuing banks that are organized and operating in the United States.
- d. Purchases of bankers' acceptances may not exceed 180 days to maturity.
- e. No more than 5% of the total market value of the portfolio may be invested in the bankers' acceptances of any one issuer.

6. Repurchase Agreements

- a. Repurchase agreements may be entered into for periods of 90 days or less.
- b. Repurchase agreements must be purchased through approved broker/dealers. All approved broker/dealers must have a signed Bond Market Association Master Repurchase Agreement on file with the State Treasurer's Office and in the case of tri-party repurchase agreements, a tri-party agreement as well.
- c. All collateral will be delivered to the Treasurer's Account at the Federal Reserve Bank or to an approved third party custodian.
- d. Overnight and open repurchase agreements must be collateralized 102% with approved securities. Term repurchase agreements must be collateralized at 102% with approved securities. The market value of all repurchase agreement collateral will be reviewed at least weekly to determine collateral adequacy.
- e. No more than 15% of the total market value of the portfolio may be invested in repurchase agreements with any one issuer.

7. Reverse Repurchase Agreements

- a. Reverse repurchase agreements may be entered into for periods of 90 days or less.
- b. Reverse repurchase agreements must be executed through approved broker/dealers. The State Treasurer's Office will assign reverse repurchase agreement trading limits for each broker/dealer.
- c. All collateral will be delivered to dealers versus payment.
- d. Collateral will be priced at market plus accrued interest. All term trades will be reviewed weekly to determine pricing adequacy.

- e. The State Treasurer's Office will enter into reverse repurchase agreements only to cover unexpected shortcomings in the Treasurer's demand account.

B. Security Selection

The following list represents the entire range of United States Agency Securities that the Missouri State Treasurer will consider and which shall be authorized for the investment of funds. Additionally, the following definitions and guidelines will be used in purchasing the instruments:

1. U.S. Govt. Agency Coupon and Zero Coupon Securities. Bullet coupon bonds with no embedded options and with final maturities of five (5) years or less.
2. U.S. Govt. Agency Discount Notes. Purchased at a discount with a maximum maturity of one (1) year.
3. U.S. Govt. Agency Callable Securities. Restricted to securities callable at par or above with a final maturity of five (5) years or less.
4. U.S. Govt. Agency Step-Up Securities. The coupon rate is fixed for an initial term. At coupon date(s), the coupon rate rises to a new, higher fixed term. Restricted to securities with a final maturity of five (5) years or less.
5. U.S. Govt. Agency Floating Rate Securities. The coupon rate floats off one index and resets at least quarterly with a final maturity of five (5) years or less.
6. U.S. Govt. Mortgage Backed Securities. Restricted to securities with stated final maturities of five (5) years or less.

C. Investment Restrictions and Prohibited Transactions

To provide for the safety and liquidity of the Missouri State Treasurer's funds, the investment portfolio will be subject to the following restrictions:

1. Borrowing for investment purposes ("Leverage") is prohibited.
2. Instruments known as Structured Notes (e.g. inverse floaters, leveraged floaters, and equity-linked securities) are not permitted. Investment in any instrument, which is commonly considered a "derivative" instrument (e.g. options, futures, swaps, caps, floors, and collars), is prohibited.
3. Contracting to sell securities not yet acquired in order to purchase other securities for purposes of speculating on developments or trends in the market is prohibited.

D. Collateralization

The State Treasurer's Office shall maintain an Acceptable Collateral Policy, which shall be consistent with State law and approved by the Governor, State Treasurer, and the State Auditor. All deposits placed in financial institutions must be at least 100% collateralized with securities listed in this policy. The Investment Committee shall periodically review and may make changes to the collateralization margins for collateral asset classes based on changes in market conditions or other events.

All securities, which serve as collateral against the deposits of a depository institution, must be safekept at a non-affiliated custodial facility. Depository institutions pledging collateral against deposits must, in conjunction with the custodial agent, furnish the necessary custodial receipts.

The Missouri State Treasurer shall have a *depositary contract and pledge agreement* with each safekeeping bank that will comply with the Financial Institutions, Reform, Recovery, and Enforcement Act of 1989 (FIRREA). This will ensure that the Missouri State Treasurer's security interest in collateral pledged to secure deposits is enforceable against the receiver of a failed financial institution.

E. Securities Lending

- a. The Treasurer may temporarily exchange securities held in the portfolio for cash or other authorized securities of at least equal value with no maturity more than one year beyond the maturity of any of the traded obligations.
- b. Securities lending may be transacted through the State Treasurer's Office custodial bank, through a third party lender, or directly with approved broker/dealers. Direct broker/dealers must have a signed Bond Market Association Securities Lending Agreement on file with the State Treasurer's Office.
- c. All securities being transferred must be delivered versus payment.
- d. Securities lending transactions may be entered into for periods of 90 days or less.
- e. The Director of Investments shall develop cash collateral investment guidelines for the reinvestment of any collateral made by the State Treasurer's Office securities lending agent and is responsible for periodic monitoring of these investments for compliance.

XII. ASSET ALLOCATION

The investment portfolio shall be diversified to minimize the risk of loss resulting from excess concentration into a specific maturity, issuer or class of securities. Diversification strategies shall be implemented through the implementation of a written asset allocation policy, which, at a minimum, outlines the minimum, maximum and target asset allocation by investment type. Target allocations indicate general objectives under steady market conditions, however targets may fluctuate throughout the year based on cash flows and market conditions. The asset allocation policy shall be established and periodically reviewed by the State Treasurer's Office Investment Committee.

XIII. SAFEKEEPING AND CUSTODY

All securities will be held by a third-party custodian designated by the Treasurer and evidenced by safekeeping receipts. All trades where applicable will be executed by delivery vs. payment (DVP) to ensure that securities are deposited in eligible financial institutions prior to the release of funds. All non-Fed eligible securities will be held at the Depository Trust Corporation through the State Treasurer's Office custodial account.

XIV. INTERNAL CONTROLS

The Treasurer has established a system of internal controls designed to prevent losses of public funds arising from fraud, employee error, misrepresentation by third parties, unanticipated changes in financial markets or imprudent actions by employees of the State Treasurer's Office. Controls deemed most important include: separation of duties, separation of transaction authority from accounting and record keeping, custodial safekeeping, clear delegation of authority, written confirmation of telephone transactions, minimizing the number of authorized investment officials, documentation of transaction strategies and a code of ethics.

XV. ADOPTION OF POLICY

The Missouri State Treasurer adopted the initial investment policy in 1993. The policy was revised in accordance with Section 30.260 R.S. Mo., (Senate Bill No. 449) in January 1998 and adopted by the State Treasurer's Office Investment Committee on January 5, 1998. The policy was last revised in accordance with section 15, article IV of the Missouri Constitution (Amendment 5) and adopted by the State Treasurer's Office Investment Committee effective October 25, 2005.

In accordance with Section 30.260 R.S. Mo., the Missouri State Treasurer shall present a copy of this policy to the governor, commissioner of administration, state auditor and general assembly at the commencement of each regular session of the general assembly or at any time the written investment policy is amended.